

Indian Economy (macro issues)

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1. Pathways for a resilient economy----GDP not a good measure

FY24GDP at 8.2%
FY23 GDP at 7.2%
FY22 GDP at 9.1%
FY21 GDP -6.6%
FY20 at 7.2%

- ✓ SIMON KUZNETS---gave GDP concept---"GDP not a welfare measure"
- ✓ Tech apps--which are free like Google maps services---not counted
- ✓ Value of non-monetized activity---"care economy"--not counted
- ✓ GDP growth not creating enough jobs--JOBLESS GROWTH
Ex --- RBI data GDP growth created 2 lakh jobs per percentage point in 1980-90, 1 lakh in 90s, now around 50k

Solutions---Green GDP, Happiness Index, Gross Env Product, **OECD's Index of Economic Welfare** (counts income distribution and pollution cost)

- o **De-growth**: shed obsession with GDP
- o Reboundary: different countries have different issues
- o Govt is good: large scale investment by govt
- o **Market not best solution**- causes cumulative causation effect-leads to increase in inequality-leads to money in hands of a few-customer centric (quote World Inequality Report)
- o Citizen centrality- justice, dignity, harmony become more imp
- o Collaborate rather than compete- like SGDs-usage of resources etc
- o Intellectual Property belongs to people-**era of knowledge economy**

Challenges affecting Global and Indian economy in 21st century (ES 23)

Cause	Affect
Pandemic	Output contraction, loss of education and income
War	Rise in price of critical commodities like oil, gas, fertiliser
Monetary tightening	Outflow of equity capital to US, dollar strengthening, CAD, slowdown in global output due to inflation
Economic slowdown in China	Zero covid policy, real estate sector turmoil

Recovery of economy

- Increase demand
- Invest for poor-like **food processing industry**-will lead to cumulative causation effect
- Increase govt expenditure-boosts animal spirits to pvt sector
- Enhance fiscal support
- Privatised public sector firms--**Gita Gopinath**
- Plug gaps in GST---"do"
- Cut wasteful expenditure from Budget--"do"

MSMEs

- ✓ Definition (for both service and manufacturing)
- ✓ Employment -11 crore (Min of MSME)
- ✓ Share in manufacturing output-35
- ✓ Share in exports- 45% (FY24)
- ✓ **Share in GVA- 27% (ES 2023)**

CLASSIFICATION	MICRO	SMALL	MEDIUM
INVESTMENT	Rs 1 cr	Rs 10 cr	Rs 50 cr
TURNOVER	Rs 5 cr	Rs 50 cr	Rs 250 cr

Issues

- Lack of registration- unregistered don't get govt benefits ---6.34 cr MSMEs in India, 99.5% are micro
- Under utilised export potential like handicrafts, handloom textiles, ayurveda etc --- Niti Aayog
- Formal credit deficit -- **banking gives less than 1/3rd credit requirement (2018 report of IFC)**
- Poor Infra--leads to low production capacity, high input cost
- Obsolete technology
- Access to mkt---ineffective ads, poor mkt channels
- IPR issues
- Pandemic impact--supply shocks
- war crisis
- Climate change

Steps taken by govt- Atmanirbhar Bharat

- Emergency Credit line guarantee --- 83% borrowers are micro (CIBIL)
- New Definition of MSMEs with inclusion of turnover criteria-more efficient
- subordinate debt scheme worth ₹20,000 cr for stressed msme
- MUDRA Yojana: interest subvention of 2% in SHISHU loans
- Champions portal for grievance redressal
- Samadhan portal for monitoring outstanding dues
- PLI
- Zero effect zero defect certification
- PMEGP
- RAMP programme---improve access to market, credit, tech
- **MSME UDYAM portal for registration**
- **Increase in GST paid by msme, surpassed FY20 level (ES 23)**

*(e-rup), e-Naira
4 Nigeria
4 e-RMB*

- Way forward
- ✓ Tie ups with MNCs
- ✓ **Ex- Amazon's Global Selling Programme (GSP)-connecting MSMEs to European and US markets**
- ✓ **Greening tech---circular** and low carbon economy
- ✓ Digitalisation
- ✓ Supply chain resilience, diversification
- ✓ Marketing--- social media influencers for targeted approach & affordable

Conclusion--- 'When India grows, world grows' --- PM

Concept of Central Bank Digital Currency---RBI defines CBDC as the legal tender issued by a central bank in a digital form.

- China--- the first major economy to launch a digital currency
- The digital currency – known as e-RMB

Advantages of digital currency

- Low handling charges—paper money eats up 1-2% of GDP
- Antidote for tax evasion, money laundering, terror financing
- Tool of financial inclusion: during emergencies, instant DBT to rural areas directly into mobile wallets
- Cashless economy— reduction in cash to gdp ratio
- Effectiveness of monetary policy
- Provides Central banks insights into purchasing patterns at citizen scale
- Faster cross border payments as No inter-bank settlement required---it would be handled by central bank directly
- Boost to digital economy — less cash economy
- Efficiency and innovation in payments
- Use of local currency in cross border payments— shield from global shocks, protect against exchange risk

Stable coin
by cryptos designed to reflect the value of fiat currencies like \$ & US

Concerns

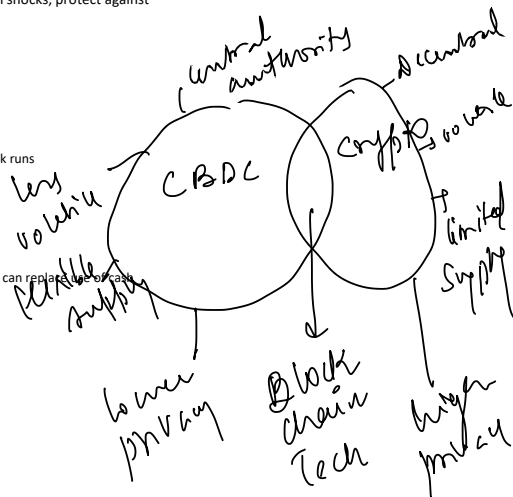
- ✓ Rise of surveillance state
- ✓ Privacy and anonymity issues— cyber hacks and threats
- ✓ Can be used to spy on movement of money
- ✓ Lack of digital literacy
- ✓ Withdrawal of deposits from banks---affects credit creations — accelerate bank runs
- ✓ Lower level of tech adoption can hinder its adoption

Recent developments

- Bank of England proposes digital sterling
- Pilot project by RBI in digital currency—India has high currency-to-GDP ratio---it can replace cash
- Union Budget 2022—Digital Rupee by RBI

Conclusion— BIS principles

Do no harm, coexistence, innovation & efficiency



CRYPTOCURRENCY (Decentralised Finance DeFi)

Context--- RBI in Financial Stability Report has called crypto a danger.
SC Garg committee--- recommended ban on private cryptocurrencies

What is cryptocurrency?

digital currencies in which encryption techniques are used to regulate the generation of units of currency and verify the transfer of funds, operating independently of a central bank.
Ex--Bitcoin, Ethereum

Bitcoin

What---trade, exchange of cryptocurrency

Why regulation?

- ✓ Anonymity issues---difficulty in regulation
- ✓ Highly volatile
- ✓ Cybersecurity
- ✓ Investor security
- ✓ No fixed border---financial crimes, terror financing, money laundering etc
- ✓ Carbon footprint---Bitcoin production estimated to generate 23 MMT CO2 emissions/ year---IEA report

How?

- Licensing
- Recognition
- Regulatory framework---define entry points etc
- Restrictions---Ex- Japan, only approved can be traded
- Detailed scrutiny---op policy, risk management etc
- KYC verification and checks of investors
- Disclosures---transparency of ops, trading, price discovery
- Record keeping---periodic inspections
- Info sharing, coordination---robust mechanism b/w regulators and law enforcement agencies

Way forward

Regulate crypto through monitored exchanges
Bring RBI digital currency as alternative

Int best practices

Canada---close monitoring, earns tax revenue from transactions

Recent developments

- El Salvador---1st sovereign country to make crypto a legal tender
- Status in India---cryptocurrency a commodity
- Govt brings Cryptocurrency and Regulation Bill 2021---ban private, launch official

FISCAL COUNCIL (FC)

What?

- ✓ independent fiscal institution to promote stable and sustainable public finances.
- ✓ independent FC appointed by and reporting to Parliament by inserting a new section in FRBM Act.

Why?

- ✓ fiscal deficit
- ✓ Recommended by 14th Finance Commission

Need for FC (fiscal consolidation, transparency,)

- ✓ transparency and accountability
- ✓ Costing of various policies to discourage populist shifts in fiscal policy and improve accountability.
- ✓ raising public awareness
- ✓ FC will work as a conscience keeper in monitoring rule-based policies

Benefits of FC (IMF study)

- ✓ stronger primary balances;

- ✓ more accurate macroeconomic and budgetary forecasts;
- ✓ raise public awareness and raise the level of public debate on fiscal policy.
- ✓ improved fiscal performances.

- Global trend
- ✓ IMF date--36 countries with IFIs in 2014
 - ✓ important tasks--
 - independent analysis
 - review and monitoring and evaluating of govt's fiscal policies and programmes
 - developing or reviewing macroeconomic and/or budgetary projections
 - costing of budget and policy proposals and programmes
 - presenting policy makers with alternative policy options

- Case Studies
- ✓ U.K.--Office for Budget Responsibility has been important in restoring fiscal sustainability.

Goods & services tax

Context

Benefits	Challenges
<ul style="list-style-type: none"> • Increased collections • Compliance & transparency-- biz with annual turnover of ₹5 cr to generate e- invoices • 1.4 cr GST payers vs 70 lakh in 2017 	<ul style="list-style-type: none"> • Cess compensation increased till March'26 • Tax rate rationalisation-- no roadmap • Non inclusion of electricity, petroleum restricts the efficiency of GST • Fake bills • Regressive tax -- burdens poor • Higher tax slabs wrt global level

Internationalisation of Indian rupee

Definition — Internationalisation of a currency (rupee here) is a process to increase rupee acceptance (credibility) across the world through cross border transaction.
 Ex— Indian rupee was legal tender in gulf nations in 1970s (gulf rupee / external rupee)

86% of India imports and exports are paid in dollars

- Pre requisites for internationalisation of currency
- ✓ Deep and liquid forex exchange market
 - ✓ Currency convert ability
 - ✓ Macro economic and political stability
 - ✓ Strong currency swap market

Pros	Cons
Cost of capital due to better access to int financial markets	Increased volatility in exchange rate in initial stages
High seigniorage benefits	Triffin dilemma— obligation of a country to supply its currency to meet global demand vs domestic monetary policies
Reduced forex requirements — more insulation from external shocks	Accentuate external shocks
Limited exchange risk / currency risk	Uncertainty in estimation of foreign demand
Higher bargaining power in international markets	

- Limitations
- ✓ India's share of global trade — only 2%
 - ✓ Rupee share in global forex markets— 1.6%
 - ✓ Rupee only partially convertible in capital account
 - ✓ Exchange rate volatility due to Current account deficit

- Concerns
- ✓ Demonetisations — shakes confidence of other countries
 - ✓ Withdrawal of currency — ₹2000

- Steps by govt
- ✓ Enable ECB in rupees
 - ✓ Vostro accounts
 - ✓ Rupee based trade with 18 countries like UAE
 - ✓ Currency swaps
 - ✓ Masala bonds

Best practices — China
 Phased approach— Renminbi

- Suggestions
- ✓ Full convertibility gradually — enhancing its liquidity
 - ✓ RBI should pursue deeper & more liquid rupee bond market — more investment options in rupee
 - ✓ Exports & imports should be invoiced in rupee
 - ✓ Currency swap agreements like with Sri Lanka
 - ✓ Tax incentives to foreign biz to utilise rupee
 - ✓ Tarapore committee— push to reduce fiscal deficits lower than 3.5% & gross NPA less than 5%

De- dollarisation

When countries tend to reduce their reliance on US currency as a reserve currency, medium of exchange and unit of account.

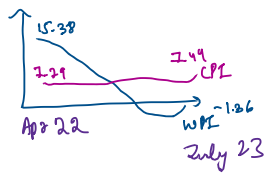
- Reasons / need
- ✓ New emerging economies — rise of Asia as economic powerhouse— Yuan, Rupee
 - ✓ Diversification
 - ✓ Promotion of local currencies— reduces foreign exchange risk
 - ✓ Macro economy affect — US manipulate global financial system for own benefits
 - ✓ Weaponisation of trade — sanctions on countries like SWIFT ban on Russia

- Initiatives for de dollarisation
- ✓ Russia-China payments
 - ✓ intra african trade using local currencies
 - ✓ India — UAE, Tanzania, vostro

- Challenges
- ✓ Unavailability of alternative currency
 - ✓ Credibility of other currencies

- ✓ Credibility of other currencies
- ✓ Trust deficit in Chinese currency

Inflation



Goldilocks scenario → Ideal state for an economy → not expanding / contracting too much.
 " Steady economic growth, preventing a recession but not so much growth that rises too much.

Impact of Inflation

Economic Impact

① On markets

- gold ↑
- stock undervalued
- purchasing power ↓
- lower real earnings

② ↓ export competitiveness

③ Income redistribution

creditors → (:-)

debtors → (:-)

④ wage-price spiral

- ... and ...

② Social Impact

→ Squeezes food budget [0 hunger]

→ child labor

→ Gendered impact: child marriage, trafficking

→ vicious cycle of poverty

(5) High C/P

(1) Income inequality R.

Institutional measures

(1) Monetary policy \rightarrow Rep rate.

(2) Fiscal policy \rightarrow GST, DBT, SAM, program tax

(3) Export \rightarrow Govt Subsidy

(4) Price Support Scheme \rightarrow PDS

(5) Monitoring mechanism \rightarrow CPI, WPI